

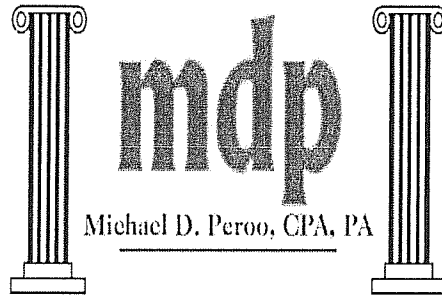
**RURAL WATER DISTRICT NO. 2
MIAMI COUNTY, KANSAS**

**Financial Statements for the
Years Ended November 30, 2010 and 2009
And Independent Auditors' Report**

RURAL WATER DISTRICT NO. 2
MIAMI COUNTY, KANSAS

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INDEPENDENT AUDITORS' REPORT

Board of Directors and Members
Rural Water District No. 2
Miami County, Kansas

We have audited the accompanying statements of net assets of Rural Water District No. 2, Miami County, Kansas as of November 30, 2010 and 2009, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards in the United States of America and the Kansas Municipal Audit Guide. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Rural Water District No. 2, Miami County, Kansas as of November 30, 2010 and 2009, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles in the United States of America.

The management discussion and analysis on pages 2 through 5 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

December 21, 2010

RURAL WATER DISTRICT NO. 2
MIAMI COUNTY, KANSAS

STATEMENTS OF NET ASSETS
NOVEMBER 30, 2010 AND 2009

ASSETS	2010	2009
CURRENT ASSETS		
Cash and cash equivalents	\$ 1,016,909	\$ 1,262,543
Certificates of deposit	997,474	3,199,340
Accounts receivable	143,810	124,764
Accounts receivable - wholesale	47,548	41,218
Interest receivable	3,811	19,317
Other receivable	31,391	-
Prepaid expenses	10,758	7,546
Inventory	94,357	106,829
Total current assets	<u>2,346,058</u>	<u>4,761,557</u>
NONCURRENT ASSETS		
Loan reserve fund	-	551,506
Funds designated for capital improvement	1,938,153	2,316,350
Bond issue costs, net	-	28,785
Total noncurrent assets	<u>1,938,153</u>	<u>2,896,641</u>
CAPITAL ASSETS		
Nondepreciable capital assets	1,224,388	633,756
Depreciable capital assets	25,636,603	25,577,968
Less accumulated depreciation	<u>(10,210,095)</u>	<u>(9,526,786)</u>
Depreciable capital assets, net	<u>15,426,508</u>	<u>16,051,182</u>
Total capital assets, net	<u>16,650,896</u>	<u>16,684,938</u>
Total assets	<u>20,935,107</u>	<u>24,343,136</u>
LIABILITIES		
CURRENT LIABILITIES		
Current maturities of long-term debt	-	267,879
Accounts payable	92,585	119,488
Other accrued liabilities	53,031	90,491
Line extension deposit	41,660	-
Advance benefit unit payments	34,500	16,500
Total current liabilities	<u>221,776</u>	<u>494,358</u>
LONG-TERM DEBT, less current maturities	<u>-</u>	<u>3,166,786</u>
Total liabilities	<u>221,776</u>	<u>3,661,144</u>
NET ASSETS		
Invested in capital assets, net of related debt	16,650,896	13,250,484
Restricted	-	551,506
Unrestricted	<u>4,062,435</u>	<u>6,880,002</u>
Total net assets	<u>\$ 20,713,331</u>	<u>\$ 20,681,992</u>

RURAL WATER DISTRICT NO. 2
MIAMI COUNTY, KANSAS

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED NOVEMBER 30, 2010 AND 2009

	2010	2009
WATER SALES	\$ 2,410,358	\$ 2,370,608
COSTS AND OPERATING EXPENSES:		
Personnel costs	562,013	553,334
Depreciation and amortization	722,441	699,754
Chemical expense	162,431	157,641
Plant expense	180,358	58,016
Line maintenance	44,774	46,167
Water purchased	72,569	54,739
Water samples	7,948	7,712
Sales and use tax	2,911	2,325
Utilities	210,984	189,499
Contract meter reading	61,757	61,597
Professional services	217,598	76,242
Vehicle upkeep	49,234	41,175
Office supplies	47,558	49,826
Insurance	24,620	21,398
Tower maintenance	5,963	47,318
Dues	15,548	16,152
Miscellaneous	11,334	10,974
Water plan tax	8,471	7,782
Bad debts	648	1,150
Clean drinking water fee	7,505	7,296
	<u>2,416,665</u>	<u>2,110,097</u>
INCOME FROM OPERATIONS	<u>(6,307)</u>	<u>260,511</u>
NON-OPERATING REVENUES (EXPENSES):		
Interest income	89,429	166,608
Interest expense	(110,735)	(132,190)
KDHE loan service fees	(14,745)	(12,699)
Miscellaneous	-	5,026
	<u>(36,051)</u>	<u>26,745</u>
INCOME BEFORE CONTRIBUTIONS	<u>(42,358)</u>	<u>287,256</u>
CONTRIBUTIONS - BENEFIT UNITS AND AID-IN CONSTRUCTION	<u>73,697</u>	<u>203,100</u>
INCREASE IN NET ASSETS	<u>31,339</u>	<u>490,356</u>
NET ASSETS, BEGINNING OF YEAR	<u>20,681,992</u>	<u>20,191,636</u>
NET ASSETS, END OF YEAR	<u>\$ 20,713,331</u>	<u>\$ 20,681,992</u>

RURAL WATER DISTRICT NO. 2
MIAMI COUNTY, KANSAS

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED NOVEMBER 30, 2010 AND 2009

	2010	2009
OPERATING ACTIVITIES:		
Cash receipts from customers	\$ 2,444,642	\$ 2,368,184
Cash payments to suppliers for goods and services	<u>(1,213,706)</u>	<u>(1,350,941)</u>
Net cash provided by operating activities	<u>1,230,936</u>	<u>1,017,243</u>
CAPITAL AND RELATED FINANCING ACTIVITIES:		
Additions to capital assets	(659,614)	(490,744)
Contributions - Benefit units and aid-in construction	73,697	203,100
Principal payments on long term debt	(3,434,665)	(257,249)
Interest and loan fees paid	<u>(125,480)</u>	<u>(144,889)</u>
Net cash used in capital and related financing activities	<u>(4,146,062)</u>	<u>(689,782)</u>
NON-CAPITAL FINANCING ACTIVITIES:		
Other non-operating receipts	<u>-</u>	<u>769</u>
INVESTING ACTIVITIES:		
Change in certificates of deposit	2,580,063	(4,096)
Interest received	<u>89,429</u>	<u>166,608</u>
Net cash provided by investing activities	<u>2,669,492</u>	<u>162,512</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	(245,634)	490,742
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>1,262,543</u>	<u>771,801</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u><u>\$ 1,016,909</u></u>	<u><u>\$ 1,262,543</u></u>
Reconciliation of Operating Income to Net Cash Provided by Operating Activities:		
Operating income	\$ (6,307)	\$ 260,511
Adjustments to reconcile operating income		
to net cash provided by operating activities:		
Depreciation and amortization	722,441	699,754
Changes in:		
Accounts receivable	(25,376)	31,830
Inventories	12,472	(14,184)
Prepaid expenses	(3,212)	805
Interest receivable	15,506	9,616
Other receivable	(31,391)	-
Other assets	551,506	-
Accounts payable and accrued liabilities	(64,363)	63,165
Line extension deposits	41,660	(20,754)
Advanced benefit unit payments	<u>18,000</u>	<u>(13,500)</u>
Net cash provided by operating activities	<u><u>\$ 1,230,936</u></u>	<u><u>\$ 1,017,243</u></u>

RURAL WATER DISTRICT NO. 2

MIAMI COUNTY, KANSAS

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED NOVEMBER 30, 2010 AND 2009

1. DESCRIPTION OF ENTITY

- a. Organization and Description of Operations – The Rural Water District (the District) was established as a tax exempt organization under the laws of the State of Kansas and is governed by an independent Board of Directors. Principal functions of the District include the acquisition, treatment and distribution of water to owners and occupants of land located within the district. Total customers at November 30, 2010 and 2009 were 3,582 and 3,572.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- a. Basis of Presentation and Accounting – The District's financial statements are presented on the full accrual basis of accounting and conform to accounting principles generally accepted in the United States of America. The District has elected under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Activities That Use Proprietary Fund Accounting*, to apply applicable GASB pronouncements, including GASB Statement No. 34, as well as any applicable pronouncements of the Financial Accounting Standards Board, the Accounting Principles Board, or any Accounting Research Bulletins, unless these pronouncements conflict with or contradict GASB pronouncements.

The accounts of the District are organized on the basis of a proprietary fund type, specifically an enterprise fund. The activities of this fund are accounted for with a separate set of self-balancing accounts that comprise the District's assets, liabilities, net assets, revenues and expenses.

The accounting and financial reporting treatment applied to the District is determined by its measurement focus. The transactions of the District are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operations are included in the statement of net assets. Net assets (i.e. total assets net of total liabilities) are segregated into invested capital assets, net of related debt; restricted for debt service; and unrestricted components.

Management of the District has made certain estimates and assumptions relating to the reporting of assets and liabilities and revenues and expenses to prepare these financial statements in conformity with generally accepted accounting principles. Actual results may differ from those estimates.

- b. Cash Equivalents – For purposes of the statements of cash flows the District considers all highly liquid debt investments having original maturities of three months or less to be cash equivalents.
- c. Inventories – Inventories consist primarily of meters, line maintenance material and chemicals. Inventories are stated at the lower of cost or market. Cost is determined using the first-in, first-out method.
- d. Loan Issue Costs – Costs related to obtaining loans have been capitalized and are being amortized on a straight-line basis over the term of the corresponding loan.

- e. Capital Assets – The cost of additions to the District’s plant, distribution system and other assets with an estimated useful life in excess of two years are capitalized. Cost includes materials, outside services and if applicable, interest on borrowed funds to finance construction. The District did not capitalize interest during the fiscal year 2010 and 2009. The cost and accumulated depreciation of property sold or retired is deducted from capital assets, and any profit or loss resulting from the disposal is credited or charged in the nonoperating section of the statement of revenues, expenses and changes in net assets.

Depreciation is calculated using the straight-line method over the estimated useful lives of the assets.

- f. Income Taxes – The District is a quasi-governmental unit, not subject to federal or state income taxes.
- g. Capital Contributions – Transmission and distribution system assets contributed to the District are capitalized at the members’ costs, which approximate fair value, and recorded as capital contributions when received.
- h. Net Assets – Net assets comprise the various net earnings from operating income, nonoperating revenues and expenses, and capital contributions. Net assets are classified in the following three components:

Invested in Capital Assets, Net of Related Debt – This component of net assets consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

Restricted – This component of net assets consists of constraints imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted – This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

3. CAPITAL ASSETS

Changes in capital assets were as follows:

	2008	Additions	Transfers/ Disposals	2009
Nondepreciable capital assets:				
Land and easements	82,203	177	-	82,380
Construction in progress	296,197	255,179	-	551,376
	<u>378,400</u>	<u>255,356</u>	<u>-</u>	<u>633,756</u>
Depreciable capital assets:				
Plant and intake	8,250,915	-	-	8,250,915
Towers and standpipe	1,047,196	-	-	1,047,196
Transmission and distribution	15,564,851	182,230	-	15,747,081
Pumps and motors	135,912	9,064	-	144,976
Office furniture and equipment	199,699	32,179	-	231,878
Vehicles	128,320	21,498	(20,011)	129,807
Equipment	15,475	10,640	-	26,115
	<u>25,342,368</u>	<u>255,611</u>	<u>(20,011)</u>	<u>25,577,968</u>
Less accumulated depreciation	<u>(8,835,936)</u>	<u>(695,107)</u>	<u>4,257</u>	<u>(9,526,786)</u>
Depreciable capital assets, net	<u>16,506,432</u>	<u>(439,496)</u>	<u>(15,754)</u>	<u>16,051,182</u>
Total capital assets, net	<u>16,884,832</u>	<u>(184,140)</u>	<u>-</u>	<u>16,684,938</u>

	2009	Additions	Transfers/ Disposals	2010
Nondepreciable capital assets:				
Land and easements	82,380	132	-	82,512
Construction in progress	551,376	590,500	-	1,141,876
	<u>633,756</u>	<u>590,632</u>	<u>-</u>	<u>1,224,388</u>
Depreciable capital assets:				
Plant and intake	8,250,915	-	-	8,250,915
Towers and standpipe	1,047,196	-	-	1,047,196
Transmission and distribution	15,747,081	20,970	-	15,768,051
Pumps and motors	144,976	7,583	-	152,559
Office furniture and equipment	231,878	3,926	-	235,804
Vehicles	129,807	21,857	(10,346)	141,318
Equipment	26,115	14,645	-	40,760
	<u>25,577,968</u>	<u>68,981</u>	<u>(10,346)</u>	<u>25,636,603</u>
Less accumulated depreciation	<u>(9,526,786)</u>	<u>(693,655)</u>	<u>10,346</u>	<u>(10,210,095)</u>
Depreciable capital assets, net	<u>16,051,182</u>	<u>(624,674)</u>	<u>-</u>	<u>15,426,508</u>
Total capital assets, net	<u>16,684,938</u>	<u>(34,042)</u>	<u>-</u>	<u>16,650,896</u>

4. CASH AND INVESTMENTS

Deposits – At November 30, 2010 and 2009, the District's deposits were covered by federal depository insurance or by collateral held by the District's agent in the District's name.

Investments – State statutes also authorize municipalities to invest general operating monies in direct obligations of the United States government or its agencies or in repurchase agreements if local financial institutions are not able to pay the average Treasury bill rate. All investments must be insured, registered or held by the municipality or its agent in the municipality's name.

The District's investments are categorized as either (1) insured, registered or securities held by the District or its agent in the District's name, (2) uninsured and unregistered for which the securities are held by the broker's or dealer's trust department or agent in the District's name (3) uninsured and unregistered for which the securities are held by the broker or dealer, or by its trust department or agent but not in the District's name. The District's investments at November 30, 2010 are summarized below:

	<u>Carrying Value</u>	<u>Market Value</u>	<u>Category</u>
Investments:			
Certificates of Deposit	\$ 997,474	\$ 997,474	1
Funds Designated for Capital Improvement:			
Certificates of Deposit	\$ 1,938,153	\$ 1,938,153	1

5. LONG-TERM DEBT

In April of 1998, the District entered into a loan agreement with the Kansas Department of Health and Environment (KDHE) to fund certain construction projects of the District, which include defined improvements to the water distribution system, and upgrading of the water treatment plant. Under the agreement, KDHE loaned \$5,515,052 at an interest rate of 4.09%. As of November 30, 2010 the outstanding balance of the KDHE loan was paid in full.

Interest expense on outstanding interest bearing obligations totaled \$110,735 and \$132,190 for the years ended November 30, 2010 and 2009.

Changes to the District's long-term debt are as follows:

	2010	2009
Total long-term debt, beginning	\$ 3,434,665	\$ 3,691,914
Principal payments	<u>(3,434,665)</u>	<u>(257,249)</u>
Total long-term debt, ending	-	3,434,665
Less current portion	<u> </u>	<u>(267,879)</u>
Noncurrent portion	<u><u>\$ -</u></u>	<u><u>\$ 3,166,786</u></u>

6. LONG-TERM WATER SUPPLY CONTRACTS AND AGREEMENTS

In connection with the original construction of the water treatment plant, a long-term contract was entered into with RWD #7 of Johnson County to provide water to that district. In addition to paying monthly charges based upon actual water usage, RWD #7 also agreed to pay an amount equal to 8.63% of the District's Water System Revenue Bonds, Series 1993. In connection with the plant expansion and the retirement of the 1993 bonds, the District amended and restated the water supply contract with RWD #7. Under the amended contract RWD #7 agreed to pay an amount equal to 10.94% of the Series 1998 Bonds.

The District also received \$333,143 in 1999 from RWD #7 for their portion of the costs associated with establishing the 1998 Bond issue which was amortized to non-operating income over a ten-year period.

In March of 2006, the District amended the wholesale water contract with RWD #7 and contributed \$337,037 for capital costs related to the water treatment plant.

In January of 2000, the District entered into a 20-year water supply contract with Rural Water District No. 1 (Miami No. 1), Miami County, Kansas. Under the agreement, the District is required to sell water to Miami No. 1 at rates based on a formula defined in the agreement.

In July of 2000, the District entered into a 30-year water supply contract with Rural Water District No. 1 (Franklin No. 1), Franklin County, Kansas. Under the agreement, the District is required to sell water to Franklin No. 1 at rates based on a formula defined in the agreement.

In July of 2003, the District entered into a water distribution contract with the City of Spring Hill, Kansas (Spring Hill) and RWD #7. Simultaneous with the water distribution contract, the District entered into a 20-year water supply contract with Spring Hill. Under the agreement, the District is required to sell water (not to exceed one million gallons per day) to Spring Hill at rates based on a formula defined in the agreement.

In February of 2006, the District entered into a 20-year water supply contract with the City of Edgerton, Kansas (Edgerton). Under the agreement, the District is required to sell water (not to exceed 250,000 gallons per day) to Edgerton at rates based on a formula defined in the agreement. Either party may, without cause, terminate the contract as of the 10-year anniversary of the contract upon 24 months prior written notice to the other party.

7. PENSION PLAN

Substantially all of the District's employees participate in the Kansas Public Employees Retirement System ("System"), a multiple employer public employee retirement system. Total payroll for employees covered by the System was \$412,469 and \$426,503 in 2010 and 2009.

Employees are vested upon hire and are required by state statute to contribute 4% of their salary (6% for employees hired after July 1, 2009) to the System. The District is required by statute to contribute the remaining amounts using the full funding method, which funds current costs each year and past service liability over a 40-year period. The District's monthly contribution rates are defined by the State and ranged from 6.14% to 7.14% in 2010. The contribution requirement for the years ended November 30, 2010 and 2009 was \$48,311 and \$41,177, which consisted of \$20,161 and \$19,566 from employees and \$28,150 and \$21,611 from the District.

The District has a 457 deferred compensation plan. Under the Plan the District matches employee contributions at rates from 2.50% to 4.50% depending upon years of service. For the years ended November 30, 2010 and 2009 the District's contribution to the Plan totaled \$13,222 and \$12,518.

8. ADVANCE BENEFIT UNIT PAYMENTS

Potential customers desiring water service within the District are required to submit an application for a benefit unit along with a deposit for the cost of a benefit unit. Such payments, refundable only if service cannot be provided, totaled \$34,500 and \$16,500 at November 30, 2010 and 2009.

9. CONTINGENCIES

The District filed suit in the District Court of Miami County, Kansas against the City of Louisburg, Kansas to recover amounts due to the District as a result of Louisburg's annexation of certain areas of the District's trade territory. The ultimate award can not be presently determined and will be recorded at the time that the amount of the award can be reasonably estimated.

10. COMPLIANCE WITH KANSAS STATUTES

References made herein to the statutes are not intended as interpretations of law, but are offered for consideration of the Director of Accounts and Reports and interpretation by the County Attorney and legal representatives of the Water District. There were no apparent statutory violations during the years ended November 30, 2010 and 2009.

11. SUBSEQUENT EVENTS

Management has evaluated subsequent events through December 21, 2010, the date which the financial statements were available for issue and determined there are no subsequent events required to be disclosed.

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